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# Supreme Court of the United States

OCTOBER TERM, 1944.

No. 513

COOPERSTOWN CORPORATION,

*Petitioner,*

*vs.*

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

## PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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# Supreme Court of the United States

OCTOBER TERM, 1944.

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COOPERSTOWN CORPORATION,

Petitioner,

*vs.*

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

## PETITION FOR WRIT OF CERTIORARI.

The petition of Cooperstown Corporation, a corporation organized under the laws of the State of Delaware, respectfully shows to this Honorable Court:

### Summary Statement of Matter Involved.

The corporate petitioner made its income and personal holding company surtax returns on the basis of cash receipts and disbursements (R. 14a). A capital stock tax return was filed by the petitioner and capital stock tax in the sum of $7,000, the amount shown due on said return, was assessed by respondent against petitioner in 1937, which was paid by petitioner in 1937 and deducted as a tax paid in its income tax return for the calendar year 1937 (R. 14a).

On April 27, 1938 petitioner filed a claim for refund of said capital stock tax on the ground that it was not engaged in business during the calendar year 1937 and was not

liable for the payment of capital stock tax for that year (R. 14a). On October 27, 1939, one year and six months after the filing of the claim for refund, petitioner was advised that said claim was allowed and petitioner received the refund on November 3, 1939 (R. 14a). The amount of that refund was accounted for by petitioner as income in its income tax return filed for the year 1939, the year in which such refund was received (R. 14a).

On March 11, 1941 respondent notified petitioner of a disallowance of the deduction taken by petitioner on its 1937 income tax return of the capital stock tax paid in that year (R. 6a, 8a). Petitioner had declared as dividends in that year more than the amount of its net income after taking the deduction for the capital stock tax of $7,000 which it had paid in that year; but through the disallowance of said $7,000 as a deduction, there resulted an undistributed net income of $4,751.24 and the imposition of a personal holding company surtax of $3,288.43 as well as an additional income tax of $1,050 (R. 10a).

Petitioner duly presented a petition for review to the Board of Tax Appeals (R. 2a-10a) and the case was tried on a stipulation of facts substantially as hereinabove stated (R. 13a, 14a).

The Board found the facts substantially as hereinabove stated (R. 16a, 17a) and decided against petitioner in a memorandum opinion, relying upon *E. B. Elliott Co.*, 45 B. T. A. 82, and *Security Flour Mills Co.*, 45 B. T. A. 671 (R. 18a).

An appeal was duly taken to the United States Circuit Court of Appeals for the Third Circuit (R. 21a-25a).

On January 19, 1944, the Circuit Court of Appeals affirmed the decision of the Board in an opinion which recognized the division of authority on the point, but which

held that, even though in this case petitioner made its returns on a cash receipts and disbursements basis so that no question of accrual accounting could be involved, the court was constrained without itself passing upon the merits to affirm the decision of the Board on the authority of *Dobson* v. *Commissioner,* 320 U. S. 489.

A petition for rehearing pointing out the inapplicability of the *Dobson* case was denied February 4, 1944; but after the decision by this Court of *Security Flour Mills Co.* v. *Commissioner,* 321 U. S. 281, the Circuit Court of Appeals granted a rehearing upon its own motion.

On August 30, 1944 the Circuit Court of Appeals filed a new opinion recognizing the inapplicability of the *Dobson* case but adhering to its original decision, upon novel grounds, in spite of what appears its manifest conflict with the decision of this Court in *Security Flour Mills Co.* v. *Commissioner,* 321 U. S. 281.

## The Question Presented.

Whether a corporation making its income tax returns on a cash receipts and disbursements basis, against which a capital stock tax was assessed in 1937 and which actually paid said capital stock tax in 1937, deducting the same on its income tax return for that year, can be deprived of that deduction because in 1938 it filed a claim for refund of said capital stock tax, which claim for refund was allowed in 1939, in which year such capital stock tax was refunded, and in which year the corporation accounted for the refund so received as part of its income for that year.

It would seem as though this issue ought to have been conclusively decided in favor of petitioner by the decision of this Court in *Security Flour Mills Co.* v. *Commissioner,*

321 U. S. 281. Nevertheless, the Circuit Court of Appeals for the Third Circuit decided otherwise not only in apparent conflict with that decision but also in conflict with the interpretation of that decision by the Tax Court in an exactly parallel case, *Stanard-Tilton Milling Co.* v. *Commissioner*, 3 T. C.—No. 127, decided June 23, 1944.

## Opinions of Court Below.

Since the opinions of the court below have not appeared in the Federal Reporter, we have printed copies thereof as an appendix to the brief accompanying this petition (*infra*, pp. 25-31).

## Statute Involved.

Revenue Act of 1936, Section 23, 49 Stat. 1658, 1659:

> "SEC. 23. DEDUCTIONS FROM GROSS INCOME.
>
> In computing net income there shall be allowed as deductions:
>
> * * * * * *
>
> (c) TAXES GENERALLY.—Taxes paid or accrued within the taxable year except— * * *."

Revenue Act of 1936, Sections 41 and 43, 49 Stat. 1666:

> "SEC. 41. GENERAL RULE.
>
> The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accord-

ance with such method as in the opinion of the Commissioner does clearly reflect the income. * * *"

SEC. 43. PERIOD FOR WHICH DEDUCTIONS AND CREDITS TAKEN.

The deductions and credits (other than the dividends paid credit provided in section 27) provided for in this title, shall be taken for the taxable year in which 'paid or accrued' or 'paid or incurred', dependent upon the method of accounting upon the basis of which the net income is computed, unless in order to clearly reflect the income the deductions or credits should be taken as of a different period. * * *"

## Jurisdiction to Review Judgment.

1. Jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended (February 13, 1925, c. 229, §1, 43 Stat. 938; January 31, 1928, c. 14, §1, 45 Stat. 54; June 7, 1934, c. 426, 48 Stat. 926).

2. Judgment of the Circuit Court of Appeals was entered January 19, 1944. Petition for rehearing was denied February 4, 1944. Thereafter, petition for rehearing was granted on the Court's motion March 2, 1944. Judgment of the Circuit Court of Appeals upon rehearing was entered August 30, 1944. This petition for writ of certiorari was filed September 27, 1944.

## Reasons Relied on for Allowance of Writ.

1. In a matter of fundamental importance to all taxpayers, as well as to the Government, the decision below relegates again to a region of doubt the application of a principle clearly restated by this Court in *Security Flour Mills Co.* v. *Commissioner,* 321 U. S. 281, by introducing

new and scarcely comprehensible distinctions and refinements to reach a result directly contrary to that demanded by the aforesaid recent decision of this Court.

The final opinion of the court below says that while under the doctrine of the *Security Flour Mills Co.* case the deduction for capital stock taken in 1937 may *not* be disallowed merely because the amount thereof was refunded in 1939, it must yet be disallowed because such refund established conclusively that in 1937 there was no legal obligation to pay the capital stock tax.

It may be pointed out that even the minor premise involved in the court's reasoning is erroneous. The Board found as a fact (R. 17a), based not only upon the parties' stipulation (R. 14a), but upon the affirmative admission in respondent's answer of that fact as alleged in the petition (R. 3a, 11a), that the capital stock tax was assessed by respondent in 1937. That assessment made the tax a legal obligation in 1937. Moreover, and secondly, in 1939, when the refund was made, the applicable statute (Internal Revenue Code, Sec. 3746) authorized the Commissioner to institute at any time within two years from the date of the refund a suit to recover tax refunds deemed to have been erroneously paid; obviously, therefore, the original non-liability of petitioner for the capital stock tax was not "conclusively established", or established at all, by the allowance of the claim for refund. The question of the original liability or non-liability of petitioner for the capital stock tax was not raised by petition or answer in the Board of Tax Appeals and was not made the subject of any finding by the Board of Tax Appeals.

From the standpoint of every taxpayer, however, and of the Government too, the major premise of the opinion below, the test of "legal liability" which the decision of

the court below superimposes upon the decision of this Court in the *Security Flour Mills Co.* case, practically nullifies that decision and certainly will be the breeder of the utmost confusion in the application of the law.

In this case the taxpayer made its income tax return on a cash receipts and disbursements basis. That basis is intended to furnish a forthright, simple basis for the determination of income tax liability, to be ascertained at the close of each taxable year on the basis of actual receipts and actual disbursements. If a tax (of the class made deductible) paid in good faith may not be deducted unless and except to the extent that it was legally imposed, then it follows that expenses paid in good faith may not be deducted if and to the extent that they may have been paid under a mistaken view as to the legal liability for their payment; and, by a parity of reasoning, sums actually received by way of income would *not* be taxable, if they were paid to the recipient under a misapprehension as to his legal right to receive them. Questions as to the correct tax liability of a person making his tax return on the simplest possible basis, that of actual receipts and disbursements, would never be susceptible of accurate determination until years later when all questions of legal liability to make payments or legal right to receive them had been finally determined.

This is not a case where one taxpayer voluntarily paid a tax assessed against another taxpayer. In that case his payment is "voluntary" and he cannot take a deduction. In the case before this Court, petitioner paid a capital stock tax for its own account which was assessed solely against itself.

It is respectfully submitted that the allowance of the writ is required not only in justice to petitioner but to prevent and forestall the introduction of a new system of judicial

distinctions undermining and destroying the doctrines plainly restated by this Court in *Security Flour Mills Co.* v. *Commissioner,* 321 U. S. 281.

2. The decision below is directly inconsistent with the decision of the Circuit Court of Appeals for the Seventh Circuit in *Nash* v. *Commissioner,* 88 F. (2d) 477, certiorari denied 301 U. S. 700. In that case it appeared that the taxpayer had erroneously paid State income taxes to the State of Wisconsin from 1926 to 1931, inclusive, under provisions of law declared unconstitutional in 1931. In each of these years he had deducted the amount of the State income taxes so paid in computing his Federal income taxes. In 1932, when his Federal income taxes for at least some of the years 1926 to 1931 were still open to review and revision, he received a refund from the State of Wisconsin of the taxes which, as it turned out, he had been under no legal liability to pay. As in the instant case, the taxpayer had made his return on the cash receipts and disbursements basis. The court held that said refund constituted income for the year in which it was received, saying at page 478:

> "It is the Commissioner's contention that a refund resulting from the return of taxes previously paid under a mistaken view of the validity of a state tax is taxable income. Reliance for this view is placed on *Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359, 51 S. Ct. 150, 75 L. Ed. 383; *Chicago, R. I. & P. Ry. Co.* v. *Commissioner* (C. C. A.), 47 F. (2d) 990; *Houbigant, Inc.* v. *Commissioner,* 31 B. T. A. 954, affirmed (C. C. A.), 80 F. (2d) 1012.
>
> We accept the views expressed in these opinions."

3. The decision of the court below is in direct conflict with the case of *Stanard-Tilton Milling Co.* v. *Commissioner,* 3 T. C.—No. 127, decided by the Tax Court of the

United States, June 23, 1944. That case involved three issues, of which the second was as follows: The taxpayer in 1935 had paid processing taxes. After the Agricultural Adjustment Act had been declared unconstitutional, it filed a claim for refund. In 1940 the claim for refund was allowed and petitioner received from the Government a refund of the processing taxes paid less the amount of unjust enrichment taxes owing by reason of such repayment. The Commissioner then assessed the taxpayer for additional income taxes for 1935, by reason of his disallowing the deduction which taxpayer (which was on an accrual basis) had taken in 1935 for the processing taxes then paid and which the Commissioner had refunded because the taxpayer had not been legally liable to pay them.

The Tax Court held that the taxpayer was entitled to retain the deduction for the processing taxes paid in 1935. The Court said in an opinion by Judge KERN (Slip opinion, pp. 4, 5):

> "The second issue is whether petitioner is entitled to deduct from its gross income for the year ended June 30, 1935, the amount of certain processing taxes which were paid by it in that year, but which, as respondent contends, were in effect refunded to it in 1940 by reason of their being credited in that year against unjust enrichment taxes agreed to be owing by petitioner. * * * Respondent urges that under the facts shown the deduction taken by petitioner in 1935 in the amount of $525,745.58 should be reduced by the amount of $32,609.35, since although the petitioner paid processing taxes in the greater amount, some part of this was, in effect, refunded in 1940 to petitioner, and, therefore, the amount of the deduction properly taken in 1935 should be adjusted by the amount of the refund granted in the later years, citing *E. B. Elliott Co.*, 45 B. T. A. 82.

> Even though we should agree with respondent's contention with regard to the divisible nature of the settlement made by the parties in 1940 under section 506, we are not able to come to the conclusion urged by him and toward which the *Elliott* case points, for we consider that the application of the principle of the *Elliott* case to the situation here presented is precluded by the recent pronouncement of the Supreme Court in *Security Flour Mills Co.* v. *Commissioner, supra.*"

The Circuit Court of Appeals in its opinion on rehearing says that the case at bar "seems plainly distinguishable" from *Stanard-Tilton Milling Co.* on the basis of the criterion that "it is necessary that the taxpayer be under a legal obligation for the payment at the time it is made or accrued". But the Commissioner of Internal Revenue made the refund to *Stanard-Tilton Milling Co.* precisely because he was of opinion at the time when he made the refund that the Milling Co. had never been under a legal obligation to pay the tax.

The fact that the court below asserts that there is a distinction between the instant case and that of *Stanard-Tilton Milling Co.* emphasizes the confusion which the decision of the court below is bound to create unless it is reviewed.

WHEREFORE, your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Third Circuit, commanding that court to certify and to send to this Court for its review and determination, a full and complete transcript of the record of all proceedings in this case numbered and entitled on its docket No. 8188, October Term, 1942,

*Cooperstown Corporation*, Petitioner, vs. *Commissioner of Internal Revenue*, Respondent, and that the said judgment of the said court may be reviewed by this Honorable Court, and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just; and your petitioner will ever pray.

COOPERSTOWN CORPORATION,
Petitioner,

By ALEXANDER B. SIEGEL,
Counsel for Cooperstown Corporation.